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IN THIS ISSUE:

Japan's Trade Surplus Declines Sharply 1

Consumption Tax Frustrates Budget Process 5

A Japanese Call For Structural Reform 6

Antitrust Action Heats Up 8

Pentagon Outlines Future Asian Pacific Defense Strategy 9

Japan Combines Cautious Action With Long-Term Environmental Plan 14

Notes: 767-X Project; Amorphous Metals 16

Japan's Trade Surplus Declines Sharply

Order the champagne or cancel the party? Potential celebrants in Tokyo and Washington could have been forgiven if they appeared a little confused by the omens presented by Japan's trade data during the early spring. The most widely cited statistic, the overall surplus on a dollar-denominated customs-clearance basis, declined 27.2 percent between 1989's first quarter and the January-March period (see Tables). Even the bilateral imbalance with the United States, which has proven more stubborn than the overall surplus, dropped 19.7 percent to the lowest quarterly figure in five years. In light of American and Japanese hopes that both the aggregate and the bilateral surpluses would contract, the figures would appear to suggest continuing improvement.

But a closer look reveals numerous problems that illustrate the difficulty of evaluating the numbers either positively or negatively. In January, for example, Japan's overall surplus practically vanished, falling to a mere $337.8 million. While relatively smaller surpluses or even deficits historically have been registered in January, this year's figure was down an incredible 89.6 percent from January 1989, when the surplus had been partly inflated by a number of temporary factors. Had Japan's trade surplus, which heretofore had been considered virtually inevitable, suddenly disappeared? Some American analysts, coming to such a conclusion, somewhat incredibly argued that such a small surplus undermined economic stability in Japan; they suggested that a slower decline would help stabilize Tokyo's stock market, then in rapid retreat. Since these same analysts tied the fate of the stock exchanges in Tokyo and New York together, they reasoned that Americans had cause to be concerned about Japan's disappearing trade surplus.

Other analysts on both sides of the Pacific pointed out the fallacy of such thinking. For starters, the stock market decline was a result of other factors, not the trade figures (see JEI Report No. 13B, March 30, 1990). Second, the declining yen -- which was linked to the stock market turmoil -- suggested that Japan's trade surplus soon could turn up again. Finally, these analysts noted, one month's figures easily could be an aberration.

The danger of drawing conclusions from one month of data was demonstrated after the release of the February and the March figures, the first of which showed a sizable drop in the overall dollar-denominated surplus on a year-to-year basis and the second a small increase. Taken together, the three sets of monthly numbers suggest very interesting developments in Japan's external sector. For example, despite the yen's relative weakness for almost the past 18 months, the volume of imports continues to show considerable growth. In the January-March quarter price-adjusted imports were running 6.7 percent ahead of a year earlier, despite sluggish growth in industrial production and in consumer spending. Similarly, export volume was up a mere 2.6 percent. Both figures suggest that the yen's near doubling in value since September 1985, a process virtually complete by early 1988, is casting a very long shadow and still may be offsetting the 20 percent or so depreciation in the currency since its all-time monthly high in November 1988.

The future of Japan's trade surplus will be determined in part by the relative effects of the yen's appreciation from 1985 to 1988 and the depreciation since then. In addition, these exchange rate factors will compete for influence with the effects of rising income levels in Japan and in that country's overseas markets, including the United States. The Japanese economy could falter badly should the weakness in the Tokyo stock market persist and interest rates remain high or rise further. Sluggish economic expansion, in conjunction with a weak yen that increasingly overpowers the effects of the currency's earlier rise in value, could suppress the growth of imports and increase both the overall trade surplus and the imbalance with the United States. In short, the news on the trade front in the first three months of 1990 was good, but continued progress is not guaranteed.

Douglas Ostrom

Japan's Total Trade in Dollar Terms

(in millions of dollars)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1985	$175,638	3.2%	$129,539	-5.1%	$46,099
1986	209,151	19.1	126,408	-2.4	82,743
1987	229,221	9.6	149,515	18.3	79,706
1988	264,917	15.6	187,354	25.3	77,563
1989	275,175	3.9	210,847	12.5	64,328
1988: I	60,279	17.1	44,505	39.2	15,774
II	65,179	14.5	47,260	29.9	17,919
III	67,169	16.1	47,258	23.2	19,911
IV	72,291	14.8	48,331	12.9	23,960
1989: I	68,227	13.2	51,142	14.9	17,085
II	67,602	3.7	51,292	8.5	16,310
III	69,595	3.6	53,048	12.3	16,547
IV	69,751	-3.5	55,364	14.6	14,387
1990: I (p)	66,689	-2.3	54,253	6.1	12,436

Japan's Total Trade in Yen Terms

(in billions of yen)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1985	Y41,956	4.0%	Y31,085	-3.8%	Y10,871
1986	35,290	-15.9	21,551	-30.7	13,739
1987	33,315	-5.6	21,737	0.9	11,578
1988	33,939	1.9	24,006	10.4	9,933
1989	37,823	11.4	28,979	20.7	8,844
1988: I	7,713	-3.1	5,688	14.7	2,025
II	8,163	0.1	5,918	13.6	2,246
III	8,924	4.9	6,280	11.3	2,644
IV	9,139	5.1	6,121	3.3	3,018
1989: I	8,705	12.9	6,516	14.6	2,189
II	9,222	13.0	6,997	18.2	2,225
III	9,911	11.0	7,547	20.2	2,363
IV	9,985	9.3	7,919	29.4	2,067
1990: I (p)	9,763	12.?	7,922	21.6	1,841

Japan's Trade with the United States in Dollar Terms

(in millions of dollars)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1985	$65,278	8.9%	$25,793	-4.0%	$39,485
1986	80,456	23.3	29,054	12.6	51,401
1987	83,580	3.9	31,491	8.4	52,090
1988	89,634	7.2	42,037	33.5	47,597
1989	93,189	4.0	48,246	14.8	44,943
1988: I	19,859	10.3	10,090	44.4	9,769
II	21,610	2.0	10,458	37.8	11,152
III	23,056	6.6	10,667	29.3	12,389
IV	25,109	10.3	10,821	25.0	14,288
1989: I	22,726	14.4	11,599	15.0	11,127
II	22,997	6.4	12,064	15.4	10,933
III	24,117	4.6	12,462	16.8	11,655
IV	23,347	-7.0	12,120	12.0	11,227
1990: I (p)	21,640	-4.8	12,709	9.6	8,931

Japan's Trade with the United States in Yen Terms

(in billions of yen)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1985	Y15,583	9.6%	Y6,213	-2.4%	Y9,369
1986	13,564	-13.0	4,918	-20.9	8,646
1987	12,148	-10.4	4,582	-6.8	7,566
1988	11,487	-5.4	5,388	17.6	6,099
1989	12,816	11.6	6,632	23.1	6,184
1988: I	2,541	-8.8	1,290	19.1	1,251
II	2,706	-10.8	1,309	20.5	1,397
III	3,063	-3.6	1,418	16.7	1,645
IV	3,177	0.9	1,371	14.4	1,806
1989: I	2,899	14.1	1,478	14.6	1,421
II	3,139	16.0	1,648	25.9	1,491
III	3,436	12.2	1,773	25.0	1,663
IV	3,342	5.2	1,733	26.4	1,609
1990: I (p)	3,168	9.3	1,856	25.6	1,312

to the earlier standard regarding exporters, which was little used. Justice expects to make a decision by fall. Depending on the scope of its finding, new legislation may be required.

In addition to these broad measures that have domestic and international implications, two recent antitrust actions focus more narrowly on bilateral issues. American businessman T. Boone Pickens appears to have opened another front in his continuing battle with Koito Manufacturing Co., Ltd., an automotive parts supplier usually identified as part of the Toyota Motor Corp. group. On April 10 his spokesman revealed that Mr. Pickens had filed with Japan's FTC a complaint claiming that Japanese automakers had forced parts companies, such as Koito, to supply products at unfairly low prices. As the largest stockholder in Koito, Mr. Pickens presumably would like to see a higher price for such parts, in possible contrast to Koito's second-largest stockholder, Toyota. Mr. Pickens claims to have letters from 50 Japanese auto parts makers charging that their customers have beaten down prices.

In a related development, both Mr. Pickens' spokesman and Capitol Hill sources revealed in mid-April that two congressional committees have requested the Federal Trade Commission to look into Japanese corporate groups centered around Japanese automakers with the objective of ascertaining whether U.S. antitrust laws have been violated. Presumably, the congressmen feel that the ties between Japan's motor vehicle manufacturers and their parts suppliers unfairly hinder free competition between American and Japanese parts producers. The FTC shares responsibility with the Justice Department for the enforcement of American antitrust statutes. Rep. Jack Brooks (D, Texas) and Sen. Ernest Hollings (D, S.C.), chairmen of the House Judiciary Committee and the Senate Commerce, Science and Transportation Committee, respectively, in late March reportedly requested the investigation, which began in early April. The congressmen asked that the findings be ready by mid-June.

These actions taken together indicate new attention to a sometimes neglected dimension of antitrust activity: extraterritorial enforcement. As such, they raise questions of conflicting laws and policies across national boundaries. While Japan often is the current focus, many of the same issues are potentially contentious between the United States, which arguably has the strongest antitrust laws, and European countries, which share what many feel is Tokyo's ambivalent attitude toward antitrust. With economic restructuring in Europe resulting from both the evolution of Eastern Europe's economy and the impending integration of the European Community, these issues eventually may have transatlantic as well as transpacific implications. In response to the emerging problem of international antitrust coordination, Professor Mitsuo Matsushita of Tokyo University already has nominated antitrust for a place on the agenda of the next round of multilateral trade negotiations under the General Agreement on Tariffs and Trade. Since the current GATT round, which began in 1986, has at least half a year to run, this suggestion, if accepted and if GATT remains a viable force, could put antitrust at the forefront of issues for years to come.

Douglas Ostrom

Pentagon Outlines Future Asian Pacific Defense Strategy

A Department of Defense official warned in testimony April 19 before the Senate Armed Services Committee that abrupt and major changes in the U.S.

security presence in the Asian Pacific would lead to regional instability. Paul Wolfowitz, under secretary of defense for policy, told legislators that whether or not the Soviets have reduced their threat in the region, the U.S. forward presence there will "remain critical to deterring war, supporting our regional and bilateral objectives and performing our military missions." The volatility and uniqueness of the East Asian environment means that America's deployment patterns should remain much as they are, particularly since they now are near the levels needed to sustain a commitment in the area, Mr. Wolfowitz emphasized.

Responding to a reporting requirement in the FY 1990-FY 1991 Defense Authorization Act, the official presented DOD's Strategic Framework for the Asian Pacific Rim: Looking Toward the 21st Century. This report discusses specific ways America's Asian allies can contribute more to regional stability as well as how the United States can reduce and restructure its military presence in the Asian Pacific. There is a growing perception on Capitol Hill that the U.S. defense budget should continue to be slashed given an apparent diminution in the Soviet threat and overall fiscal pressures.

However, a major thrust of Mr. Wolfowitz's testimony was that the Asian Pacific is not Europe; defense cutbacks that might be appropriate for the European arena, given Moscow's weapons and force reductions and the nascent political reform movement in Eastern Europe, are not analogous to East Asia's situation (see Table 1). Political volatility and turbulence will characterize important regional players, such as China, the Soviet Union, North Korea, Cambodia and the Philippines, he pointed out. Moreover, while the Soviet Union has been withdrawing some aircraft and ships from Southeast Asia, Moscow continues to modernize its weapons systems. In the Soviet Far East military district that fronts Japan, in particular, Soviet capabilities still appear "to far exceed those needed for defense," ensuring a continued threat to U.S. and allied interests in Northeast Asia, Mr. Wolfowitz stated (see Table 2).

Table 1: U.S. Forward-Deployed Forces

Command	Total Personnel	Forward Deployed	Percent of Total Force[1]
Europe	341,000	341,000[2]	16.0%
Pacific	362,000	135,000[3]	6.3
Other Noncontinental U.S. Commands	34,000	34,000[4]	1.6

[1]Total force is 2.13 million.
[2]This number includes 21,000 personnel afloat.
[3]This number includes 25,000 personnel afloat but does not include 8,000 personnel assigned to Guam.
[4]This number includes 12,000 deployed to Africa and Near East/South Asia; 21,500 deployed to the Western Hemisphere; and 500 stationed in the Soviet Union, Eastern Europe and Antarctica.

Source: Department of Defense

While urging a continued, substantial air and naval presence in the Asian Pacific, the Pentagon nevertheless is acutely aware of budgetary

realities. DOD therefore has proposed measured reductions of some ground and air forces in South Korea, Japan and the Philippines, reductions that it believes will not destabilize the region. The Pentagon's 10-year, phased-in plan would decrease troop strength by 14,000 to 15,000 service personnel (out of the total 135,000 deployed in the Asian Pacific) during the first three years. The next three to five years would see proportionally greater reductions in combat forces undertaken incrementally to "ensure that potential adversaries do not misread our deterrent capability and intentions." Modest cuts beyond the second phase of reductions would continue during the remaining years, given then existing circumstances. The phased approach would allow the United States to remain flexible and responsive to changes in regional conditions, Mr. Wolfowitz stated.

Table 2: Soviet Forces in Asia

Ground Forces	
Maneuver Divisions	48
Artillery Divisions	3
Tanks	11,500
Artillery	12,500
Helicopters	1,100
Pacific Fleet	
Total Ships, Vessels and Craft	875
Ballistic Missile Submarines*	26
Attack Submarines	94
Carriers	2
Cruisers	11
Destroyers	8
Frigates	56
Minor Combatants	202
Amphibious	21
Support and Miscellaneous Craft	455
Combat Aircraft and Helicopters	345
Naval Infantry Divisions	1
Air Forces	
Bombers	215
Fighters/Attack Aircraft	890
Air Defense Fighters	590

*This is a combined total for conventionally powered and nuclear-powered ballistic missile submarines.

Source: Department of Defense

Another key theme in the Pentagon's report concerns the critical importance of the U.S.-Japan relationship, described as the "linchpin of the U.S.-Asian security strategy." DOD stresses that it is in the U.S. interest to maintain a forward-deployed presence in Japan over the long term because of the

strategic location of bases and the cost effectiveness of the U.S. presence there compared to elsewhere. However, Pentagon strategists recognize that over the next decade U.S.-Japan relations most likely will continue to be strained by trade disputes and fears over the loss of American technological competitiveness. In addition, the merits of the U.S.-Japan security relationship no doubt will continue to come under fire by some Japanese who favor either a more neutral posture or, conversely, a more nationalistic approach to defense. Outraged by the persistent U.S. trade deficit with Japan, a growing number of American legislators also no doubt will call for a cutback in the U.S. presence -- and military dollars spent -- in Japan unless Tokyo shoulders far more of the mutual defense burden.

Thus, DOD believes that the following elements should guide American defense policymaking toward Japan:

- The U.S. force level should be reduced as much as possible while maintaining essential bases that enable this country to help provide regional stability and deterrence in Northeast Asia.

- The United States should continue to encourage Japan to increase its territorial defense capabilities and enhance its ability to defend its sea lanes out to 1,000 nautical miles, while at the same time discouraging the development of an expanded reach that would threaten its neighbors rather than help maintain stability.

- Japan should be urged to participate more closely in political efforts with Western allies to maintain stability in key regions of the world as well as encouraged to support Asian Pacific adjustments.

- Tokyo should be encouraged to increase its financial support for U.S. forces operating in Japan.

- Maximum procurement from the United States should be advocated to maintain interoperability of military systems.

- Increased technology flowback should be pressed, while Japanese development of noncomplementary systems should be discouraged.

- The bilateral security consultative process should be revitalized.

DOD's proposed multiphase reductions for the Asian Pacific region notwithstanding, the United States would continue to have substantial air and naval capabilities in Japan while possibly trimming ground and some support air forces, particularly in Okinawa; approximately 5,000 to 6,000 personnel stationed in Japan would be withdrawn during the first three years. Current deployment patterns on mainland Japan would be little changed; the U.S. Air Force presence would be maintained at Misawa and a forward-deployed carrier would be kept at Yokosuka (see Table 3). DOD also plans to make adjustments to U.S. bases and facilities at Okinawa with the aim of returning property to improve civilian-military relations.

In the second cutback phase the Japan Self-Defense Forces would be encouraged to improve qualitatively through procurement of advanced weapons systems and streamlined infrastructure for command, control and logistics. The

Table 3: U.S. Troops Deployed in Japan

Bases

Main Islands

- Yokota (Headquarters, U.S. Forces Japan; Headquarters, Fifth Air Force)
- Zama (Headquarters, U.S. Army IX Corps)
- Yokosuka (Headquarters, U.S. Naval Forces Japan)
- Sasebo (Naval fleet base)
- Atsugi (Naval air station)
- Iwakuni (Marine Corps air station)
- Misawa (Air base; naval air unit)

Okinawa

- Kadena (Air base; naval air unit)
- Camp Courtney (Marine Corps camp)
- Futenma (Marine Corps air station)

Troop Strength

Army	2,400
Navy	6,850
Air Force	16,200
Marine Corps	24,700
Total	50,150

Source: Department of Defense

United States also plans to pursue further reductions in the Asian Pacific contingent on regional stability and its allies assuming more responsibilities.

The final period could see still further reductions in U.S. forces stationed in Japan. However, the Pentagon believes that no matter how stable the region or sophisticated the Japanese self-defense capability, the United States must maintain "deterrent capabilities" in Japan, such as a home-port aircraft carrier, strategic lift aircraft and an air force capability to carry out surgical strikes.

In the area of cost sharing Mr. Wolfowitz stated up-front that Washington expects increased assistance from all its allies, not just Japan. But he warned Congress to avoid the temptation of decreeing a certain level of gross national product or other specific criteria as constituting a "fair share" of the defense burden. "Arithmetic formulas for increases based solely on the premise that there are significant trade imbalances or simply that a specific ally should 'do more because it has the money' will likely be met with stiff resistance because such approaches can be viewed as challenges to national sovereignty," the DOD report states. Congress last year passed legislation that requires the administration to negotiate with Tokyo to achieve Japanese security contributions equal to 100 percent of the direct costs of maintaining the

U.S. forces based on the island nation (see JEI Report No. 38A, October 6, 1989). In the past legislators also have proposed that Japan be required to spend 3 percent of its GNP on defense (see JEI Report No. 19A, May 13, 1988).

Barbara Wanner

Japan Combines Cautious Action With Long-Term Environmental Plan

An April 17-18 global environmental conference in Washington blended environmental and economic concerns, but the mix proved volatile, initially igniting criticism from many of the European participants, who urged more action rather than more study. Left out of most reports about the 17-nation conference, which attempted to achieve more serious consideration of the economic impacts of dealing with global climate change, were measures described by the Japanese delegation, led by Environment Agency director general Ishimatsu Kitagawa.

Although the Japanese voiced lofty goals, such as a 100-year plan to reduce carbon dioxide emissions, other policy statements appeared to echo the American theme of more study, which may have been why the U.S. media appeared to overlook Japan's presence. For example, a position paper available at the conference included a statement from June 1989 by the Ministers for Global Environmental Conservation, a group of 19 high-level Japanese officials. "It is vital to strive for the protection of the global environment, while assuring the stable development of the world economy . . .," the outline read. The chumminess of the Bush administration with the Japanese on this issue surfaced in Environmental Protection Agency administrator William K. Reilly's speech, which singled out the Japanese for their "ambitious and imaginative commitments" to address global warming through research and development of new technologies over the next 100 years.

The 100-year plan, developed by the Ministry of International Trade and Industry, accepts the idea that levels of carbon dioxide are mounting worldwide. Scientists generally do not dispute this but rather disagree over whether this increase will result in the warming of the earth's atmosphere, which could affect weather patterns and coastlines and bring about a variety of other potentially hazardous consequences. Since proposals to cut down CO_2 invariably address industrial and automotive emissions of the gas, the economic impact of a cutback could be staggering.

Some estimates put the cost to the U.S. economy of a 20 percent reduction in CO_2 emissions at $800 billion to $3.6 trillion over 100 years, depending on how much technology and clean alternative energy is used. Souzaburo Okamatsu, director general of MITI's industrial location and environmental protection bureau, summarized a Japanese study at the White House conference that said a cutback of 20 percent in CO_2 emissions over the next 10 years could result in a 0.4 percentage point decline in the worldwide gross national product rather than an initially projected gain of 1.5 points. Just a freeze on carbon dioxide emissions at 1989 levels could result in world economic stagnation, he warned, adding that most of the impact would be felt by developing nations. MITI's plan basically aims at stabilizing Japan's CO_2 emissions in the next 50 years and gradually phasing them out before 2090.